

School Finance Statistics and the U.S. Supreme Court: Theory and Reality

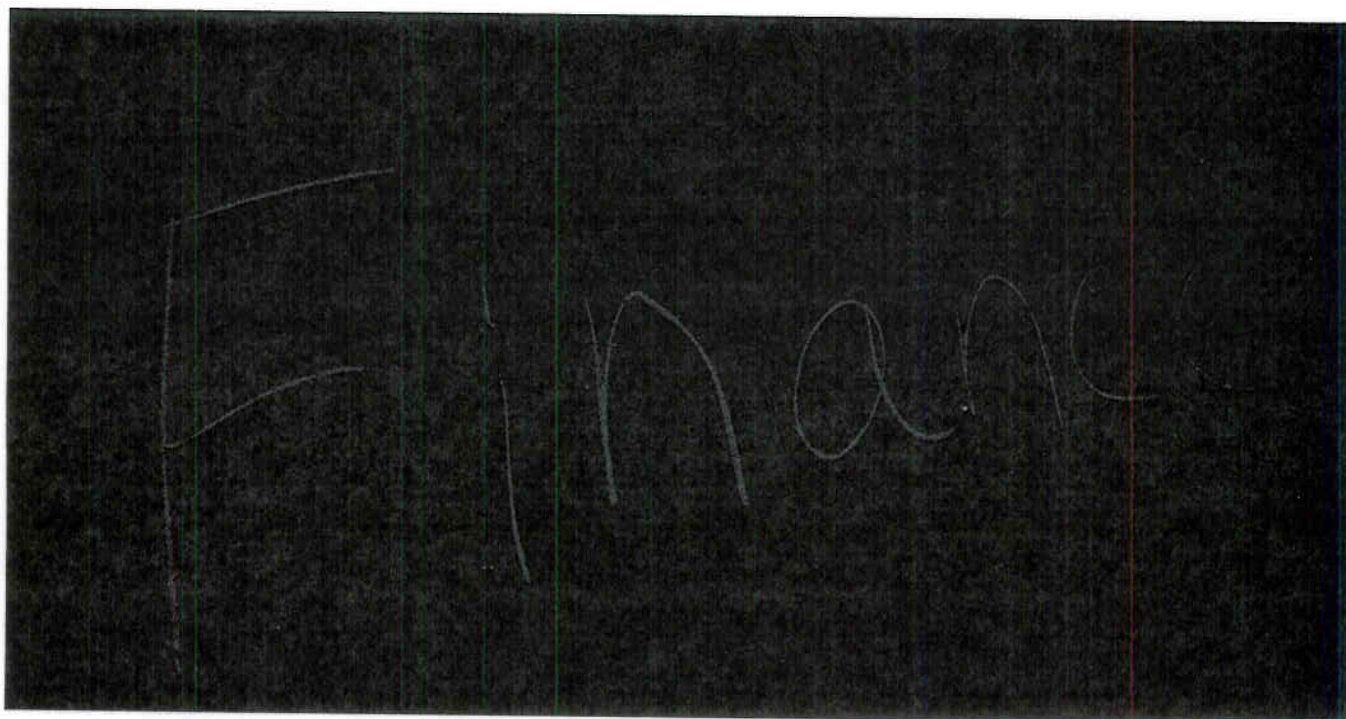
As a professor who regularly teaches a class on school finance, I rarely have the opportunity to link the theoretical school finance statistics I teach about in class with real-world situations that affect the operating budgets of local school districts. The U.S. Supreme Court's ruling in *Zuni Public School District 89 v. U.S. Department of Education* (2007) provided just such an opportunity.

In what seems like an esoteric ruling in support of the U.S. Department of Education, the Supreme Court upheld the way the department computes a statistic that determines how states can treat districts that receive federal Impact Aid. Although it affects only a few states right now, efforts to improve school finance equalization over time may result in more states and districts facing the choices made by New Mexico.

The statistic in question, known as the federal range ratio (FRR), is used to determine the relationship of the per-pupil revenue of low-revenue school districts to high-revenue districts in a state. To compute the FRR, the revenue of the 5th percentile district is subtracted from that of the district at the 95th percentile and then divided by

the revenue of the district at the 5th percentile. This computes the difference in revenue as a percentage of the revenue in the lowest (5th percentile) revenue district. The typical equity standard for an FRR computation is 0.25, or 25%. That means that the difference between the high- and low-revenue per-pupil districts must be 25% or less than the revenue of the low-revenue district.

The FRR is computed using districts at the 5th and 95th percentile of per-pupil revenue to avoid distortions that can be caused by outlier districts with unusually high or low per-pupil revenues. More importantly, computation of the districts at the 5th and 95th percentiles should be based on pupil counts, not district counts. That means that when the computation is performed, districts enrolling 90% of the students in the state are included in the computation. Depending on the size and revenue level of school districts across a state, if district percentiles were used, it would be possible to include either substantially more students and districts in the calculation (if most of the outlier districts are small) or considerably fewer than 90% of the students in the state if one or two very large districts have particularly high or particularly low per-pupil revenues.



By Lawrence O. Picus, Ph.D.

My students routinely ask why anyone would care about a statistic like the FRR, and many don't understand why I am so concerned with computing the FRR on a per-pupil rather than a per-district basis. I'm certain they would be surprised to learn that the issue was a matter of consideration before the U.S. Supreme Court and that the opinion hinged almost entirely on the basis by which the FRR should be computed.

On April 17, 2007, the FRR and pupil versus district computations were exactly what the Court addressed in its ruling in the *Zuni* case. For two districts in New Mexico, the ruling meant they would be unable to receive additional state funds to operate their schools.

The *Zuni* case grew out of a dispute in New Mexico over the disparity test used to determine whether a state's finance system was equalized. This is important to school districts that receive federal Impact Aid (as well as other forms of federal aid). Federal Impact Aid is provided to school districts that are unusually affected by actions of the federal government, and it is intended to replace local revenues that are lost because the federal government pays no property taxes on the land it owns.

In general, federal Impact Aid cannot be deducted from the revenue that states send to local school districts. The exception is cases in which the state's funding formula is determined to equalize expenditures for free public education among local education agencies in the state. If the FRR is 25% or less, the federal government considers the state's funding formula equalized and allows states to consider federal Impact Aid receipts when distributing resources to local school districts.

New Mexico is one of three states that meet this standard, as computed by the U.S. Department of Education. As a result, New Mexico deducts an amount equal to 75% of the federal Impact Aid that districts receive from their state aid. The 1,585-student Zuni Public School District and the 13,000-student Gallup-McKinley County Public Schools sued the U.S. Department of Education, claiming that the way the secretary of education computed the FRR resulted in a determination that the FRR for New Mexico was below 25%; consequently, they did not receive as much state revenue as they were entitled to receive. Since federal Impact Aid amounted to \$8.1 million in Zuni and \$26.8 million in Gallup-McKinley, a substantial amount of money was on the table.

The case hinged on the way the districts at the 5th and 95th percentiles were determined. The districts claimed that the Department of Education wrongly used the number of pupils (rather than the number of districts) to compute the percentiles, omitting 23 of the state's 89 school districts, and that a strict interpretation of the statute creating this exemption from the use of federal funds made it clear that the assistant secretary of education should have used a district count and omitted only 10 districts (which enrolled only 1.8% of the state's students).

The difference is significant because if computed as the districts argued, the FRR for New Mexico would have

exceeded 25%, and the state's funding system would not have been equalized. As a result, New Mexico would not have been able to reduce each district's state revenues by 75% of the federal Impact Aid receipts.

In a five-to-four decision, the Supreme Court held that the secretary's interpretation of the statute—which essentially disregarded language stating that district counts, not pupil counts, should be used—was acceptable because it was a logical approach to calculating the FRR and because it had been done that way for years. Moreover, the justices concluded that there was a strong statistical rationale for using the calculation the secretary had chosen.

So why does this matter to school business officials? Understanding esoteric and unique school finance computations can matter in any state. Had the districts prevailed, they would have been able to receive more than \$6 million and more than \$20 million, respectively, in additional state revenues.

And there is one more issue that may require further adjudication. Throughout this discussion, I have referred to the computation of the FRR (and I would argue any other school finance statistic) on the basis of school district revenues. The statute and the U.S. Department of Education's regulations all refer to revenues as well. Yet, the Court stated, "We also disregard the statute's frequent references to local 'revenues' because those references do not raise any additional considerations germane to this case" (*Zuni*, p. 18).

Yet, every school business official knows that there is always a difference between revenues and expenditures (hopefully a positive one when expenditures are subtracted from revenues). More importantly, that difference may not be uniform across all school districts. As a result, small differences in the share of total revenues that actually result in expenditures from year to year could cause slight differences in the computation of the FRR. If the computation is close to the standard of 25%, it is possible that calculations with both expenditures and revenues could cause the value of the FRR to be on both sides of the 25% standard. So, while not an issue now, it may become one in time.

Many of my students may still question the importance of the FRR (and of other school finance statistics I teach them), but I'm sure every school business administrator whose district receives large amounts of federal Impact Aid will have a new appreciation for the ways in which the FRR is computed. ■

References and Resources

- Odden, A. R., and L. O. Picus. 2008. *School finance: A policy perspective*. 4th ed. New York: McGraw-Hill.
- Zuni Public School District 89 v. U.S. Department of Education*, 550 U.S. ____ (2007).

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